

## **MINUTES**

**BOARD OF TRUSTEES OF THE  
PUBLIC EMPLOYEES' RETIREMENT FUND  
143 West Market Street, Suite 500  
Indianapolis, IN 46204  
September 13, 2002**

### Trustees Present

Jonathan Birge, Chair  
Richard Doermer, Vice Chair  
Teresa Ghilarducci  
Steven Miller  
Nancy Turner

### Others Present

Richard Boggs, Burnley Associates  
Stephanie Braming, William M. Mercer Investment Consulting  
Micah Fannin, William M. Mercer Investment Consulting  
Lisa Erb Harrison, Ice Miller  
Bart Herriman, Executive Assistant to the Governor  
Pete Keliuotis, SIS  
Stephanie Rhinesmith, Special Liaison to the Governor for Public Finance  
Curt Smith, SIS  
Michele Solida, Indianapolis Star  
Doug Todd, McCready & Keene, Inc.  
E. William Butler, PERF Executive Director  
Caroline Drum Bradley, PERF Internal Auditor  
Donavan Cartwright, PERF Call Center  
Diann Clift, PERF MIS Director  
Jo Duncan, PERF Investment Officer  
Patricia Gerrick, PERF Chief Investment Officer  
Ed Gohmann, PERF Legal Counsel  
Patrick Lane, PERF Communications Director  
Doug Mills, PERF Chief Financial Officer  
Tom Parker, 1977 Fund Director  
Ken Stoughton, PERF HR Director  
Lynda Duncan, Minute Writer

## ITEMS MAILED TO THE BOARD PRIOR TO THE MEETING

- A. Agenda of September 13, 2002 Meeting:
- B. Minutes:
  - ❑ July 12, 2002 Board of Trustees Meeting
  - ❑ August 23, 2002 Board of Trustees Meeting
  - ❑ June 14, 2002 Investment Committee Meeting
- C. Reports, Summaries, Memoranda and/or Letters Concerning:
  - ❑ Line-of-Duty Death Determinations (2)
  - ❑ Call Center Update
  - ❑ PERF Draft Policies
  - ❑ Class Action Suits/Bankruptcies Resolution
  - ❑ Member Reporting Charts
  - ❑ DROP Seminars
  - ❑ Alternative Investments – Commitment Recommendation
  - ❑ Schedule of Administrative Expenses and Investment Fees

A quorum being present, the meeting was called to order.

### 1. MINUTES APPROVAL.

**MOTION** duly made and carried to approve the Minutes of the July 12, 2002 meeting of the Board of Trustees.

*Proposed by:* Steven Miller  
*Seconded by:* Nancy Turner  
*Votes:* 5 for, 0 against, 0 abstentions

**MOTION** duly made and carried to approve the Minutes of the August 23, 2002 meeting of the Board of Trustees.

*Proposed by:* Nancy Turner  
*Seconded by:* Teresa Ghilarducci  
*Votes:* 5 for, 0 against, 0 abstentions

### 2. DISCLOSURES.

Mr. Doermer – Bank One stock ownership. PERF holds a detailed listing of all of shares owned by Mr. Doermer

### 3. EXECUTIVE DIRECTOR'S REPORT.

- Line of Duty Death Determination. The Board members were reminded that according to the statute, the definition of the state employee line of duty death benefit refers to a death that occurs as the direct result of personal injury or illness resulting from the state employee's performance of the duty of the employee's job.

**MOTION** duly made and carried to approve the award of a line-of-duty death benefit in the case of Bonnie S. Pelligrino, former highway maintenance for the Indiana Department of Transportation, who died as a result of a work accident that occurred on July 17, 2002.

*Proposed by: Steven Miller*  
*Seconded by: Jonathan Birge*  
*Votes: 5 for, 0 against, 0 abstentions*

It was noted that the case of Mr. Thomas Minor had been deferred for review at a future Board meeting.

- Actuarial Audit Update. Mr. Gohmann advised that Milliman, the firm employed by PERF to carry out the actuarial audit, had been waiting for some raw number data files from PERF. This data together with past asset reports had now been provided. Work accomplished so far involved a background review of the data provided by the actuary and samples of actuarial valuations provided by PERF's current actuary. A team from Milliman would meet with PERF staff on September 24, 2002 to address any remaining issues. Parallel valuations for the 1977 Fund and PERF will be reconstructed in order to compare current actuarial valuations and to verify if the assumptions and methodology used by PERF's actuary were appropriate. It anticipated that their report would be available by November.
- Employment Policies. Policies had been provided to the Board for review and would be discussed at the Board's October meeting.
- Employer Advisory Group (EAG). Mr. Lane advised that on August 21, 2002, the EAG had met for the fifth time. The EAG currently meets on a quarterly basis. The Outreach Services Director, Mr. Prizevoits, is establishing individual contact with employers in order to improve interaction.

❑ Agenda items included:

- Brief discussion of the dismissal of Kevin Scott;
- Diann Clift, Management Information Systems Director, gave an update on electronic reporting and data clean up. It is anticipated that the data clean-up project would require increased employer participation.
- A progress report on the Call Center.
- An update on two benefit enhancement initiatives (interim payment of 85% retirement benefit and deferred withdrawal of the Annuity Savings Account on retirement).

- Mr. Lane noted that the City Controller of Indianapolis had made some recommendations on internal processes in relation to the Kevin Scott issue and had provided some points of contact in credit rating agencies. Ms. Ghilarducci asked if there had been any sense of how employers and members were reacting to the issue. Mr. Lane considered that the events were too new at the time of the meeting to have provided a reaction. Ms. Ghilarducci recommended that a letter should be sent out from the Board of Trustees to PERF's membership, to include the following elements:

- Events that had occurred in the Kevin Scott case;
- Reassurance that benefits are safe;
- Expression of concern on the part of the Trustees and assurance that they will be kept informed of developments;
- Provision of a point of contact for members (e.g. Call Center) with any questions or concerns about this issue.

Mr. Miller considered that the fund participants had already absorbed some bad news this year in the investment funds. Although the investment losses did not impact on the basic retirement benefit, this had still generated some concern among the members. Their pension benefit is established by law and is not affected by investment losses. Some assurance was required.

Mr. Birge noted that there were several on-going projects, e.g. the investigation by the Governor's Office and the forensic audit, as well as several different law enforcement agencies and sensitivities. This would require coordination.

Mr. Lane noted that very few phone calls on the Kevin Scott issue had been received from members by the Call Center. Callers had been reassured their pensions were secure in a defined benefit guaranteed by law.

- Call Center Update. Mr. Cartwright, Call Center Manager, provided an update on the Call Center Operation. Mr. Butler noted that the Call Center had been established on May 15, and results for a quarter period were now available, and aimed to provide a highlight of experiences so far.

- Mr. Cartwright noted that 25 calls had been received related to Kevin Scott incident. Typically, calls had not been directly concerning Kevin Scott, and callers had contacted PERF on other issues, and would mention this in passing. More calls had been received following the Enron and Worldcom situations.

- The call volume was cyclical, and largely driven by benefit checks and statement runs, etc.
- Staffing levels appear to be appropriate. Temporary employees had performed well and it was advocated that, in the long term, these positions should become permanent. Ms. Ghilarducci noted that the temporary employees do not receive benefits.
- Call Center Graphs. June and July benefit checks were issued slightly late resulting in increased call center activity. In August, quarterly statements were issued and there was general concern about the changes in the Guaranteed Fund rate for members' Annuity Savings Accounts, losses experienced by other funds, and concern over the economy. Most people call about refunds and retirement. Non receipt or delayed receipt of checks generate increased call volume. During the computer system changeover period in July, approximately 1,400 calls were received in one-day.
- Information was provided on performance with regard to how quickly a member's call is answered average and waiting times. Generally, 78% of calls are answered within 25 seconds. This information is provided using real time software. Talk time is generally four minutes.
- E-mail volume. Inquiry forms are available on the PERF website. Response time to these inquiries is approximately four hours. One full-time employee handles e-mail inquiries.
- Call Center personnel are responsible for sending out forms to members. The change of address form, refund packets and direct deposit forms are the most commonly requested.
- Future Projects. Call Center representatives have started a cross training program with other PERF departments. On-line access to PERF's policies and procedures is being developed. On-going work includes data clean up and quality improvement initiatives.

Mr. Doermer noted that this was a very professional operation. He asked if many calls were received from people asking to change their investment mix. It was noted that members had an option to change their investment direction each quarter by means of the investment direction change form sent out with the quarterly statements. It was noted that calls concerning the change in the Guaranteed Fund rate had generally been positive. Mr. Birge congratulated the Call Center staff for contributing to achieving a dramatic improvement in PERF's services. This had been an area where PERF had been criticized in the past. Mr. Miller commended Mr. Butler and Mr. Lane for bringing this project to fruition.

Ms. Turner asked if PERF used RIPEA to advantage for communication with the retired members. It was recommended that a summary of the Call Center briefing should be sent to them. Mr. Butler noted that he would be attending the RIPEA Annual Convention on September 16 and he would speak about this.

4. LEGAL ISSUES.

- Resolution. Mr. Gohmann provided a draft resolution 02/-3 that would authorize PERF staff to continue to take any necessary action to protect PERF's rights, plans and securities relating to class action suits and bankruptcy proceedings. He noted that a number of new class action suits had been filed in 2002. This would ensure that the appropriate pleadings were submitted and information on class certification received in order to file the appropriate proof of claims to ensure that PERF will be part of any recovery of assets. This did not imply that PERF would be the lead plaintiff, but would be a member of the class that was certified.

**MOTION** duly made and carried to adopt resolution 02/-3 as presented.

*Proposed by: Steven Miller*  
*Seconded by: Teresa Ghilarducci*  
*Votes: 5 for, 0 against, 0 abstentions*

5. BENEFITS. Mr. Butler provided an update on member record reporting. He noted that there are essentially three major types of data that flow through PERF: new member's records, retirement applications, and refund applications.

- New member records are applications for new membership. Application forms are completed with information provided by the employee and the employer. Approximately 2,000 applications are received each month. This includes people that are already PERF members but who have changed jobs and are required to submit a new record under their new employer. Processing involves imaging the record, setting up member accounts, and verifying the accuracy of the information provided. Problems encountered in processing the applications due to missing or incorrect information. This is a fairly labor intensive requirement in order to image and set up the information correctly. The purpose of the data clean-up project had been to establish a policy to keep the data as "clean" as possible before going forward in order to avoid problems being encountered later on.
- Refund applications tend to be seasonal (e.g. peaks due to seasonal employment or the school calendar). In spite of a slight increase in inventory from July to August, numbers are being held steady and it is anticipated that the backlog will gradually be eliminated.

- Approximately 500 retirement applications are received each month. Processing numbers in May were low, due to problems with the implementation of SIRIS. Progress was made in June and in July and August. However, figures are now heading in the wrong direction. A total of 556 applications were received in May and only 116 were processed. PERF is concentrating on trying to improve the process. The refund application comprises 14 pages incorporating information from the employee and employer. A number of applications received each month are rejected because they are incomplete but can remain 30 to 45 on file at PERF before the defect is noted and the file is returned to the employee or employer for correction. The goal will be to collapse some of these processing times. The Pension Management Oversight Committee was instructed by the Legislative Council to inquire into that particular issue.
- ❑ Ms. Ghilarducci noted that the goals would take time to implement. PERF had no Chief Benefits Officer (CBO), and as identified in the strategic plan last year, the largest problem areas in the Fund were identified as occurring in the benefits area. She advocated moving forward quickly to replace Kevin Scott. Mr. Birge acknowledged that the intention was to replace Mr. Scott but considered that it was important not to move forward with rehiring until appropriate background check procedures had been established. Mr. Birge stated that he anticipated that Mr. Bowman's report would be ready in the near future, and should provide necessary guidance. He noted that the situation had been disappointing because PERF had started to accomplish some of its goals, particularly in the benefits area.
- ❑ Mr. Miller considered the CBO position was critical to PERF's operations and recommended that the hiring process should be started as soon as possible. It would not be necessary to get to the background check phase until candidates had been identified. It was agreed that Mr. Birge would contact Mr. Bowman and the Governors Office to confirm when the report would be provided. He believed this would be soon. Mr. Miller considered if the report was delayed, then the Board should move forward with the hiring process regardless. Obviously, PERF would comply with any hiring procedures or background checks identified by the Governor's Office, but he considered that PERF had a responsibility to keep the Fund moving in order to protect our membership. Ms. Ghilarducci noted that PERF had another eight or nine critical staffing needs that also needed to be addressed. She recommended commencing the advertising process and to have interviews set up before the next Board meeting in October. Mr. Butler confirmed that these positions remained critical to PERF's operation. Additionally, new requirements were surfacing, particularly with respect to PERF's new custodial arrangements. Eight positions had been approved in the Board's 2003 budget. The State hiring freeze commission had approved seven of the eight new positions, in addition to filling vacated "backfill" positions and to converting temporary positions

to fulltime positions. Mr. Birge considered that it was important to determine what kind background checks are to be done before PERF started to employ people. Ms. Ghilarducci asked if the other State agencies continued to hire personnel.

- ❑ Ms. Turner advocated reinstatement of regular Benefit Administration Committee meeting.
- ❑ Mr. Doermer noted that the scope of the background checks would probably extend to many more than in the past and beyond PERF also.
- ❑ Ms. Ghilarducci considered that the Board should defer to the professionals to carry out the investigations, but that as Trustees, it was important to determine what was needed as a Fund to serve employers and members. Mr. Miller asked if the senior positions could be recruited through an executive recruiting firm. Mr. Butler noted that a background check was what you made of it, and you get what you ask for and what you paid for. PERF had initiated some discussions with a private firm regarding carrying out appropriate background checks for PERF positions. Mr. Miller recommended using an executive agency search in terms of delivering four or five qualified candidates, and then to focus on background checks. It was noted that positions that merited intensive background checks had been identified. It was acknowledged that PERF had access to an enormous amount of highly sensitive information that required safeguarding. Ms. Ghilarducci noted that other State agencies had access to sensitive information and asked if PERF had been singled out as having an employment process that was different from the rest of the State.

It was agreed by the Board members to defer to Mr. Birge's proposal and wait for the results of the inquiry before taking any action to fill the vacancies. Mr. Birge was cognizant of the concerns the Board members and agreed that discussion would be revisited if it appeared that the process would be longer than anticipated. Mr. Birge noted that he was very hopeful that PERF would soon be in a position to move forward. He further noted that this process may also prove to be useful to other levels of State government.

6. POLICE AND FIRE. Mr. Parker advised that the 1977 Fund Advisory Committee had met on August 19, 2002. During the meeting, the following items were addressed:

- Line-of-duty death benefit claim. The committee had affirmed the local board recommendations concerning four duty-related disability determinations. One of the recommendations resulted in a decision that the disability was not duty-related and the Committee affirmed the local board's denial. Letters of determination confirming those decisions will be issued from PERF.



- Deferred Retirement Option Plan Seminars. Over 600 members had attended the seminars so far this year and feedback had been positive. Mr. Butler noted that Mr. Miller, Chairman of the Committee, had expressed his appreciation of the DROP team panel including Mr. Gohmann, Mr. Swank, Mr. Osborn, and Mr. Parker.
- Issues to be raised at the Pension Management Oversight Commission (PMOC) meeting in October (benefit enhancements and presumptive issues). Mr. Parker noted that the Committee had discussed a proposal to change the base salary from First Class Salary to the salary for the last three years and how this would impact the Fund. Mr. Todd, actuary for the Fund, noted that studies had been done in the past, but they had not used actual salaries because only First Class Salaries were reported. Results of the analysis were 21% and 6%. He noted that salaries vary by cities and towns, and that the First Class Salary is generally lower. He will do the study using salaries provided by the Indianapolis Police and Fire departments in order to find out from them what the salaries were at the time of retirement and compare with the first class salary. Ms. Ghilarducci asked if South Bend could also be used for the study. Mr. Gohmann noted that the Fraternal Order of Police (FOP) had raised this issue at the Committee meeting and it was not known whether a recommendation would be made by the Committee to take this to PMOC this year.
- The Committee discussed a recommendation to do a survey of 1977 Fund members.
- They received a presentation from the Northern Indiana Computer Transportation District Chief indicating their interest in participating class in the 77 Fund.

7. INVESTMENTS. The Investment Committee had met earlier that morning. Agenda items had included:

- A review of the investment performance presented by Mercer. It was noted that it had been a difficult year, particularly for equity markets, and managers had performed as well as could be expected. Indexing had been adversely affected because the index funds fell into the lower half of performance. The fund, within its universe of public funds, was basically right in the middle.
- Burnley Associates presented a review of compliance results. There had been nothing out of line to note. It was noted that PERF's fixed income managers tended to invest heavily in corporate issues. It was the sense of the Investment Staff that PERF does not have the resources to properly monitor these securities. This is due to a lack of in-house systems. However, it was anticipated that these tools would, to a great extent, become available

following completion of the custodial search. In addition, PERF did not have the staff to run the tools and the Chief Investments Officer (CIO) indicated that additional staff would be necessary to perform this function. This item will be raised in more detail at a future board meeting.

- Barclays Global Investors (BGI) Presentation. The presentation had addressed the issue of equity risk premiums. This presentation provided necessary background information for Trustees as PERF progressed with its asset liability study. The presentation also covered return enhancement strategies.
- Searches in Progress. The CIO provided an update on searches in process:
  - ❑ Global Custody Search. Requests for Proposal (RFPs) are due on September 26. Finalists will be interviewed on November 8.
  - ❑ Global Equity Search. Managers are required in core and growth strategies. PERF retained Brandes as a global value equity manager. Finalist interviews will take place on October 10 and 11.
  - ❑ The CIO summarized the transition activities that have been made to date to fund the managers that have been hired. Funding should be completed next month.
- PERF's large cap enhanced index fund is currently managed by UBS. The international enhanced index is managed by State Street. It was the sense of the Investment Committee that better returns and efficiency could be achieved by moving index and enhanced index equity assignments to BGI. The Investment Committee was recommending to the Board to terminate State Street and UBS and to transfer those assets to BGI.

**MOTION** duly made and carried to terminate State Street and UBS and to transfer those assets to BGI.

*Proposed by:* Teresa Ghilarducci  
*Seconded by:* Jonathan Birge  
*Votes:* 5 in favor, 0 against, 0 abstentions.

- Consecro Capital Management. Due to the deteriorating situation of Consecro Capital Management, PERF's Staff and Consultant had recommended immediate termination of the Consecro relationship. The recommendation was implemented following discussion of concerns with the Board and Investment Committee Chairman. The Investment Committee affirmed termination of the relationship with CCM. This decision had been regrettable since CCM was an Indiana based corporation.

**MOTION** duly made and carried to endorse the Investment Committee's affirmation of the termination of PERF's contract with Conseco Capital Management and that these assets (approximately \$200 million) should be transferred to Western Asset Management.

*Proposed by:* Steven Miller  
*Seconded by:* Nancy Turner  
*Votes:* 5 for, 0 against, 0 abstentions.

- Presentation by House Investments. This is an Indiana-based real estate and investment firm forming a limited partnership fund targeting capital commitments of \$100 million. Their chief investment area is the midwest and Indiana, and it is the recommendation of the Investment Committee that PERF commit an amount equal to 15% of the eventual fund not to exceed \$15 million. In addition, the Fund's total commitment cannot exceed \$100 million. Mr. Miller noted that the required due diligence work had been accomplished successfully and he commended PERF's consultants and internal staff on their effective and thorough procedures.

**MOTION** duly made and carried to commit an amount equal to 15% of the eventual fund, and not to exceed \$15 million, to the limited partnership fund of House Investments. The Fund size cannot exceed \$100 million.

*Proposed by:* Richard Doermer  
*Seconded by:* Teresa Ghilarducci  
*Votes:* 5 for, 0 against, 0 abstentions

- BackTrack is an investigative service to be used to carry out extensive background research on prospective investments. This had not been necessary for Lindsay, Goldberg and Bessemer because PERF had not been the lead investors and there has been extensive background done on them already. House was PERF's first major institutional investor and PERF would be the lead investor. Therefore it was appropriate ensure that this was included in the due diligence list of firms for this particular assignment. Ms. Ghilarducci noted that it would have been preferable to employ Indiana firm unless it compromised the investment procedures.

**MOTION** made and carried to include approve the recommended additions to the Fund's special services roster. BackTrack was selected for this particular investigative assignment.

*Proposed by:* Steven Miller  
*Seconded by:* Richard Doermer  
*Votes:* 5 for, 0 against, 0 abstentions

- Central Indiana Life Science Initiative. This is an initiative to develop a vehicle for raising venture capital commitments directed primarily towards Indiana investments. Their last meeting had included an expanded group of

potential limited partners. A list of terms was provided to give structure to the composition of the fund. It was noted that some of the corporate participants have different objectives to the pension fund and foundation participants. Goals on what the fund will and can accomplish are being defined. PERF agrees with the potential investors supporting a smaller fund size due to venture capital opportunities, particularly if focussing on life sciences in Indiana, because there is not the desired volume. The goal of the fund is to create opportunities. Some potential limited partners consider that the fund needs to be big enough to attract venture capitalists to the region. There is a large difference of opinion on what the appropriate fund size should be. Other investors are hesitant to invest large amounts into areas that are not of sufficient size to generate attractive long-term returns. Further details will be provided at PERF's October Board meeting. Another issue will be how this fund will be managed. Initially, one of the ideas was to have this manager or professional fiduciary that would be separate from the general partners. This is unusual because normally the general partner is the same as the fund manager, and concerns that this arrangement might limit some of the deal flow and loss of control of the process, as well as deter potential managers. Baker and Daniels have been tasked to research if these two roles can be separated. Potentially, this initiative offers a vehicle to fulfill safely and responsibly some of their desires to invest in Indiana and still be able to meet fiduciary responsibilities. Between now and the next Board meeting in October, it is the intention to finalize some of those terms and provide a firmer list of potential LPs that might participate in the fund.

- Future Items. The following items will be addressed at the next Investment Committee meeting:

- Information on Duke investment
- Review of SIS and contract extension
- Distressed debt.

- Ms. Gerrick noted that Lindsay Goldberg and Bessemer had their third closing and are now at \$1.8 billion. A capital contribution adjustment of \$18,000 in interest has already been received resulting from new investors coming into the fund.

8. AUDIT AND BUDGET. Mr. Doermer noted that he and Nancy Turner constituted the Audit and Budget Committee and were charged with the responsibility of overseeing the audit and developing a budget that is submitted to the Board for final approval. At the Audit and Budget meeting held that morning, the following items were discussed:

- Audit Report.

- ❑ The State Board of Accounts Audit. This is on schedule and the final report is expected at the end of October 2002.
- ❑ Actuarial Audit. This is expected to be received in November.
- ❑ Forensic Audit. There is nothing to report there except that it is underway.
  - ❑ Audit plan schedule and the audit for this year for our own internal audit work under Caroline Bradley's supervision. An additional audit had been added to the 2002 audit plan for 1977 Fund benefits processing. Some reprioritization may be required to accommodate the time currently being spent on the forensic audit.
  - ❑ Audit Survey. Ms. Bradley distributed to the Audit Committee a survey carried out by the Association of Public Pension Fund Auditors that had involved several other states and provided a comparison of the composition and procedures of their respective audit committees. PERF's Audit Committee had compared favorably.
  - ❑ Change of the audit committee communications report format. Ms. Bradley advised that she was working on finalizing the format.
- Budget Report. Mr. Mills noted that the Board had been provided schedules with listings by cost center of actual expenses compared to budget (for 2 months of the FY 02 to date). These results are tracked on a cash basis. He noted that some of the expenses listed including salaries, benefits and actuarial fees, included expenses that would eventually be accrued into the FY 02 actuarial results. Therefore the FY 03 figures are favorable to the budget. Nothing significant had been noted for the first two months of the year.

## 9. OTHER BUSINESS.

- Oath of Office. Each Trustee signed an Oath of Office that was notarized by Ms. Gettle. The Oaths of Office will be filed with the Secretary of State.
- Information Items. Mr. Butler noted that several information items had been included at the back of the Board Books.
  - Letter of recognition from the Government Finance Officers' Association for excellence in PERF's annual financial report. Several suggestions had been made for improvement to the presentation and this will be taken into consideration. The FY 02 financial report is in the process of being prepared and should be ready by October 15, 2002.

- Mr. Gohmann also noted that a letter had been received complimenting Ms. Montgomery, PERF Retirement Counselor, on her professionalism and helpfulness.
10. EXECUTIVE SESSION. The Board met in Executive Session under IC 5-14-1.5-6.1(b)(6).
  11. NEXT MEETING. The next regularly scheduled meeting of the Board will be held on Friday, October 11, 2002 at 1:00 p.m.
  12. ADJOURNMENT. There being no further business, the meeting was adjourned.